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**UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN FRANCISCO DIVISION**

In re:

PG&E CORPORATION

-and-

**PACIFIC GAS AND ELECTRIC
COMPANY,**

Debtors.

- ☐ Affects PG&E Corporation
- ☐ Affects Pacific Gas and Electric Company
- ☒ Affects both Debtors

**All papers shall be filed in the Lead Case,
No. 19-30088 (DM)*

Bankruptcy Case
No. 19-30088 (DM)

Chapter 11
(Lead Case)
(Jointly Administered)

**OPPOSITION OF THE OFFICIAL
COMMITTEE OF TORT CLAIMANTS
TO MOTION OF DEBTORS PURSUANT
TO 11 U.S.C. §§ 105(a), 363(b), AND
503(c) FOR ENTRY OF AN ORDER (I)
APPROVING DEBTORS' INCENTIVE
PROGRAM FOR CERTAIN KEY
EMPLOYEES AND (II) GRANTING
RELATED RELIEF (Dkt. No. 2664)**

Date: July 24, 2019
Time: 9:30 a.m. (Pacific Time)
Place: United States Bankruptcy Court
Courtroom 17, 16th Floor
San Francisco, CA 94102

The Official Committee of Tort Claimants (“**TCC**”) in the chapter 11 cases (“**Bankruptcy Cases**”) of the above-captioned debtors and debtors-in-possession (collectively, hereafter the “**Debtors**”) hereby submits its Opposition to the Motion of Debtors Pursuant to 11 U.S.C. §§105(a), 363(b) and 503(c) for Entry of an Order (I) Approving the Debtors’ Incentive Program for Certain Key Employees and (II) Granting Related Relief (the “**KEIP Motion**”), and respectfully represent as follows:

I. SUMMARY OF ARGUMENT

Neither the California Legislature, the California Public Utilities Commission (“**PUC**”) nor the United States District Court for the Northern District of California (“**District Court**”) are satisfied that the Debtors have adequately prioritized the safety of the gas and electricity systems they operate. Each of these oversight bodies has found that this convicted felon and criminal offender has egregiously neglected public safety. The Court has not been presented with justification to reject the serious concerns of every party that is charged with overseeing the Debtors’ operations, and to simply rubber stamp its senior management bonus program.

The senior management bonuses requested through the KEIP Motion are yet another example of business as usual at PG&E. Either the incentive plan should be rejected in its entirety, or approved only upon the conditions that (1) the performance metrics are revised to a 100% weighting on safety, and (2) the senior management incentive payments may be disgorged if, during the performance period, (a) the Debtors cause a catastrophic wildfire that results in one or more fatalities, or (b) if either the District Court or the PUC find that the Debtors have engaged in more lies relating to or a cover-up of their safety performance.

II. STATEMENT OF RELEVANT FACTS

AB 1054

On July 12, 2019, the State Assembly passed AB 1054, the “Public utilities: wildfire and employee protection” bill. By any reasonable evaluation, the bill is an extraordinary measure designed to stabilize the major investor owned utilities (“**IOUs**”) in California, particularly the debtor, Pacific Gas and Electric Company, the largest IOU in the State.

1 AB 1054 is a lengthy and complicated bill, the full discussion of which is beyond the
2 scope of this memorandum. The relevant point for these Debtors' right to propose a business as
3 usual bonus plan is this: The history of the Debtors' safety record is so abysmal that the State of
4 California has decided that it must step in and remove management's discretion with regard to
5 wildfire safety. Specifically, AB 1054 calls for the establishment of a California Wildfire Safety
6 Advisory Board and a Wildfire Safety Division of the PUC. Under new Public Utilities Code
7 §8389(b), the board shall make recommendations to the division on, among other things,
8 "[a]ppropriate performance metrics and processes for determining an electrical corporation's
9 compliance with its approved wildfire mitigation plan," and "[t]he appropriate scope and process
10 for assessing the safety culture of an electrical corporation."

11 Moreover, the legislation has teeth where it comes to executive incentive compensation.
12 Section 8389(e) authorizes the PUC director, commencing as of June 30, 2020, to issue a safety
13 certificate to an electrical corporation, if the electrical corporation provides documentation of,
14 among other requirements, that "[t]he electrical corporation has established an executive
15 compensation structure approved by the division and structured to promote safety as a priority
16 and to ensure the public safety and utility financial stability with performance metrics, including
17 incentive compensation based on meeting performance metrics that are measurable and
18 enforceable, for all executive officers [as defined]. *This may include tying 100 percent of*
19 *incentive compensation to safety performance and denying all incentive compensation in the*
20 *event the electrical corporation causes a catastrophic wildfire that results in one or more*
21 *fatalities.*" (Emphasis added.) Although the statute will not come into effect until June 2020, and
22 is therefore not yet binding on the Debtors and this Court, the message from the state government
23 to place safety above all other metrics is clear.

24 **PUC – 18-12-007 PG&E Locate and Mark Order Instituting Investigation ("OII")**

25 The PUC initiated the OII in December 2018, and the probe is continuing. A status
26 conference has been set for July 30, 2019, at 1:00 p.m. This investigation arises from the
27 aftermath of the San Bruno gas explosion that destroyed a neighborhood and killed eight people
28 in 2010. It was commenced after an investigation by the PUC found that the Debtors had

1 falsified records for five years. Under California law, the Debtors were required to locate and
2 mark their natural gas pipelines in a timely manner. Apparently, as they fell behind in meeting
3 their safety requirements, the Debtors pressured supervisors and contractors to falsify data so that
4 the locating and marking would not appear as late. In the OII proceeding, the PUC is considering
5 the penalties it will impose on the Debtors for their violations. This proceeding is not business as
6 usual for a well-run IOU: The Debtors—the State’s largest IOU—lied to regulators for years, all
7 while under criminal investigation.

8 **District Court Criminal Probation Proceeding**

9 As the Court is aware, Honorable William Alsup, United States District Judge for the
10 Northern District of California, is presiding over a criminal probation of the Debtors arising from
11 the San Bruno fire and the Debtors’ conduct in its aftermath.

12 Just days ago, on July 10, 2019, the district court ordered the Debtors to respond to a new
13 Wall Street Journal story claiming that the Debtors knew for years that its power lines that
14 ultimately caused the 2018 Camp Fire were deficient and that they intentionally failed to perform
15 upgrades. (The Butte County District Attorney also has commenced a criminal investigation in
16 connection with the Camp Fire.) The Debtors’ detailed response to the order is due on July 31,
17 2019.

18 Judge Alsup also questioned the Debtors’ decisions to pay over \$5 billion in dividends
19 and millions in campaign contributions during the same time frame, while ignoring unsafe
20 conditions.

21 The proceedings identified above, together with the catastrophic damage and loss of life
22 that occurred as a result of 18 fires in 2017 and 2018 that the Debtors’ equipment started, are the
23 context in which the Court must review the proposed KEIP.

24 **III. ARGUMENT**

25 The Debtors recite that Section 503(c)(3) of the Bankruptcy Code permits payments to
26 employees outside the ordinary course of business when those payments are justified by the facts
27 and circumstances of the case. They say that this standard is “determined by application of the
28 same business judgment standard utilized under Section 363(b) of the Bankruptcy Code.” The

1 familiar corporate law prism that this standard invokes is the business judgment rule, which is
2 premised on the Debtors’ directors’ discharge of their fiduciary duties of care and loyalty. (The
3 Debtors recognize this, as well, on page 21 of their motion.) Importantly, the particular action
4 that is required to discharge those duties is context-driven, that is, is driven by the facts and
5 circumstances – the reality – prevailing when the action is taken. *See Malone v. Brincat*, 722
6 A.2d 5, 10 (Del. 1998) (“Although the fiduciary duty of a . . . director is unrelenting, the exact
7 course of conduct that must be charted to properly discharge that responsibility will change in the
8 specific context of the action the director is taking”); *McMullin v. Beran*, 765 A.2d 910, 918
9 (Del. 2000) (the contours of the common law fiduciary duties directors must discharge “depends
10 on the specific context that gives occasion to the board’s exercise of its business judgment”);
11 *North American Catholic Educational Programming Foundation, Inc. v. Gheewalla*, 930 A.2d
12 92, 101 (Del. 2007) (*quoting Malone v. Brincat* passage quoted above); *Marchand v. Barnhill*,
13 2019 WL 2509617, at *15 (Del. 2019) (though directors have great discretion to tailor context-
14 specific approaches to their companies’ businesses and resources, they must make a good faith
15 effort to address “central compliance risks”). Nothing in the bankruptcy law repeals these
16 precepts.

17 The incentive plan at issue here is not the Debtors’ 2019 STIP, which covers thousands of
18 their rank-and-file employees. The plan at issue is the Debtors’ proposed 2019 KEIP, whose
19 participants are “their most senior officers whose performance would have the greatest impact on
20 the Debtors’ operations [and] safety . . .” and who “are largely responsible for the Debtors’
21 ongoing day-to-day operations and . . . overall business strategy.” (KEIP Motion at 9). The
22 KEIP participants, say the Debtors, “are vital to the Debtors’ safety, operations and revenue-
23 generating capacity.” (KEIP Motion at 7). In short, the KEIP participants are the people who set
24 the priorities and direction for the STIP participants, and who set and manifest the “tone at the
25 top” of all of the Debtors’ endeavors.

26 The context for the Debtors’ proposed KEIP, which cannot responsibly be brushed aside,
27 is that the Debtors are on criminal probation because of public safety failures that resulted in
28 fatalities, and that subsequent to their criminal convictions, the Debtors committed additional

1 safety violations that resulted in more fatalities. The horrific consequences of the Debtors’
2 enduring and pervasive pattern of safety violations, some of which occurred under the proposed
3 KEIP participants’ leadership, are what led the Debtors to initiate these bankruptcy proceedings
4 and to the need for the motion that we are addressing. That is the present reality.

5 And yet somehow, though it seems nearly inconceivable, the Debtors move for approval
6 of a KEIP designed and presented as if this context – reality – simply did not exist. They proceed
7 blithely as if they were just one of so many “peers” that somehow has had the misfortune to find
8 itself in bankruptcy proceedings, with only the faintest nod to the public safety failure millstone
9 that dominates its, and the Northern California public’s, current and future fate. Some
10 observations from the Debtors’ motion will illustrate the point.

11 The Debtors formulated the KEIP together with their advisors and the Compensation
12 Committee of PG&E’s board of directors (which committee now comprises two hedge fund
13 leaders and a utility industry consultant). (KEIP Motion at 9). The “Debtors believe that the
14 KEIP’s design and scope is reasonable . . . and that its implementation reflects a sound exercise of
15 the Debtors’ business judgment.” (KEIP Motion at 8-9). The Debtors’ lead advisor, Willis
16 Towers Watson (“WTW”), a compensation consulting firm, believes that “the KEIP’s design is
17 reasonable when compared to the Debtors’ peer group and consistent with market practice.”
18 WTW “undertook a comprehensive analysis of the KEIP” (KEIP Motion at 11).
19 Elaborating on WTW’s analysis on their behalf, the Debtors noted that WTW conducted a
20 benchmarking analysis “of 21 companies with revenues greater than \$1 billion that recently
21 implemented KEIPs in Chapter 11” and evaluated data from “a sample of 19 peer companies . . .
22 approved by the Compensation Committee, published survey compensation data for [those]
23 companies, published survey data for the broader energy services industry, and published survey
24 data for general industry companies.”

25 The declaration of Douglas J. Friske, a Managing Director at WTW, filed with the
26 Debtors’ motion, lists the items WTW discussed with the Debtors at the start of WTW’s
27 engagement: “the Debtors’ operational history, financial performance, and various issues
28 regarding the Debtors’ workforce and employee programs.” WTW also reviewed the Debtors’

1 “existing base salary and primary incentive programs, paying specific attention to the incentive
2 plans’ performance metrics [and] participating employees.” *See* Declaration of Douglas J. Friske
3 in Support of Motion of Debtors Pursuant to 11 U.S.C. §§ 105(a), 363(b), and 503(c) for Entry of
4 an Order (i) Approving Debtors’ Incentive Program for Certain Key Employees and (ii) Granting
5 Related Relief (“**Friske Declaration**,”) at 4). Mr. Friske notes that the KEIP was designed to
6 reflect “the unique circumstances of this case, taking into consideration typical market practices
7 in both restructuring scenarios as well as normal course, [sic] utility industry practices.” (Friske
8 Declaration at 11).

9 The Debtors’ motion and supporting declarations make it amply clear that “peer”
10 comparisons and “market” practice have carried the day. The only thing missing from the KEIP
11 efforts that the Debtors choose to highlight and emphasize is a reflection of the proposed plan’s
12 context, i.e., any discernible recognition whatsoever of the Debtors’ safety posture and solutions
13 as issues of overriding importance in everything they do, including how they incentivize those
14 who control their strategy and day-to-day operations.

15 In another presumably unintended confirmation of the Debtors’ “business as usual”
16 approach, the target KEIP awards are based on “the historical STIP and LTIP target award
17 values,” specifically on the target awards approved by the Debtors’ pre-filing compensation
18 committee in December 2018. (KEIP Motion at 10). But here comes the safety nod: the KEIP
19 weights “safety metrics” at 65%, financial (earnings from operations) performance at 25%, and
20 customer satisfaction at 10%. The safety metrics components are: nuclear reliability and safety,
21 5%; first-time inspection of gas transmission pipeline miles, 10%; documentation of electric and
22 gas construction projects, 10%; corrective action in response to employee or contractor injuries or
23 fatalities, 15%; and the public safety index (“**PSI**”) (relating to circuit miles of vegetation cleared
24 and circuit miles of system hardening completed), 25%. If the threshold level public safety index
25 metrics are not met, the overall KEIP payout that would otherwise be made will be reduced by
26 50%; if the threshold level public safety index metrics are met but the target level ones are not,
27 the overall KEIP payout will be reduced by 25%. (KEIP Motion at 12-13). Last but perhaps not
28 least, the Debtors tell us that the “KEIP Performance Metrics are not easily achievable or

1 ‘layups’” and that the “PSI Metric . . . is subject to revision if the California Public Utilities
2 Commission requires changes.” (KEIP Motion at 16). And the Board or Compensation
3 Committee can eliminate payment of the KEIP awards completely, in their discretion, even if the
4 performance targets are met. (KEIP Motion at 8).

5 So the Debtors have checked the safety box. What’s not to like? Well, in the context of
6 an incentive compensation plan for the executives who will determine and direct the public safety
7 outcomes of a company that is on criminal probation for public safety violations, even a slightly
8 closer examination of the Debtors’ KEIP presentation raises a number of troubling issues
9 regarding the Debtors’ purportedly “sound” exercise of their business judgment.

10 First, the Debtors tout the KEIP’s weighting of safety at 65%. But the reality is that the
11 only metric that attaches legitimately to wildfire safety (the problem that brought us here; *see*
12 above) is the public safety index. Its weighting is 25%, exactly the same as – not higher than –
13 the earnings from operations metric. In glaring contrast to the Debtors’ proposed KEIP plan, AB
14 1054 sets the safety metric at up to 100%. Second, the KEIP was formulated by the Debtors’
15 Compensation Committee and the Debtors’ advisors. Nothing in the Debtors’ motion or in the
16 supporting declarations refers to any consultation with the Debtors’ Safety and Nuclear Oversight
17 Committee, the PUC, or with any other safety expert or authority.

18 Third, the Debtors and WTW congratulate themselves on having a “PSI Modifier” that
19 would effect the payout reductions that we describe above. But in the Debtors’ and Northern
20 California public’s wildfire safety context, the more valid and salient description of the modifier
21 is that even if the Debtors fail to achieve the threshold PSI metrics, the KEIP participants will still
22 get 50% of their aggregate KEIP payout. And if the Debtors eke over the threshold PSI metrics
23 level but fail to reach the target PSI metrics level, those participants will still get 75% of their
24 aggregate KEIP payout. To say the least, this hardly signifies giving priority to the issue that will
25 most affect the Debtors’ financial survival and the financial and other outcomes for the Debtors’
26 stakeholders.

27 Fourth, the Debtors’ claim that the KEIP performance metrics are not easily achievable is,
28 simply, not verifiable based on the information that the Debtors have provided in their motion or

1 supporting declarations. The Debtors keep telling us that the metrics are not easily achievable:
2 they keep not telling us essentially anything about what those metrics are, and keep not telling us
3 anything at all about what makes the metrics difficult to achieve. The Debtors’ related statement
4 that the PSI metrics are subject to revision “if the California Public Utilities Commission requires
5 changes” obviously provides no reassurance concerning the Debtors’ appetite for developing
6 public safety incentives that are not imposed on them externally. And the notion that a Debtor
7 board or Compensation Committee can (but is not obligated to) eliminate KEIP payouts entirely
8 is almost as useful as Oscar Wilde’s observation that the rich and poor alike can sleep under
9 bridges.

10 A brief review of the *Marchand v. Barnhill* case cited above is instructive here. The
11 plaintiff in that case sued the directors of the Blue Bell ice cream company for breach of their
12 fiduciary duties in failing to monitor recurrent listeria problems in the company’s production
13 system. Those problems ultimately led to three fatalities. In ruling that the plaintiff had made
14 viable allegations of fiduciary duty breaches, the court observed that “[i]n Blue Bell’s case, food
15 safety was essential and mission critical.” The court noted further that “. . . a corporate board
16 must make a good faith effort to exercise its duty of care. A failure to make that effort constitutes
17 a breach of the duty of loyalty.” For the Debtors, public safety, encompassing most visibly
18 wildfire safety, is “essential and mission critical.” The Debtors’ directors are not on trial with
19 respect to the proposed KEIP. But the proposition that their duties of care and loyalty mandate
20 including heightened measures to incentivize public safety in a KEIP for their executives, in the
21 context of the Debtors’ public safety history and current posture, cannot responsibly be brushed
22 aside.

23 In summary, the Debtors’ artfully crafted proclamations about their devotion to public
24 safety in the design of their proposed KEIP are a thin veneer – one that they hope will mask their
25 stubbornly persistent dismissiveness of public safety concerns. It no doubt will take more than
26 requiring a KEIP design that prioritizes safety appropriately to change the Debtors’ safety culture.
27 But at each turn, it is incumbent on the Debtors, their constituents, and those otherwise positioned
28 to affect the Debtors’ affairs, to face and deal with the reality of the facts and circumstances that

1 dominate their current condition and to demand discharge of their boards' fiduciary duties with
2 the required full recognition of those facts and circumstances. The Debtors are companies that
3 have a badly broken safety culture, and this court should require that any KEIP that it will
4 approve will in fact prioritize, and demonstrate that it prioritizes, public safety above all other
5 considerations. The KEIP that the Debtors now propose for approval fails utterly to do that, and
6 approval of it will endorse the Debtors' boards' breach of their fiduciary duties and send utterly
7 the wrong message to the Debtors and their constituents.

8 **IV. CONCLUSION**

9 The Debtors' motion for approval of the proposed KEIP should be denied.

10
11 Dated: July 17, 2019

Respectfully submitted,

12 BAKER & HOSTETLER LLP

13 By: /s/ Cecily A. Dumas
14 Cecily A. Dumas

15 *Counsel to the Official Committee of Tort*
16 *Claimants*